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# Economic Intelligence Weekly

**Secret**

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12 March 1975

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# ECONOMIC INTELLIGENCE WEEKLY

12 March 1975

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## Overview

The Spreading World Recession is taking its toll of the international trade of the major developed nations. Trade volume has sagged in recent months, and the downward trend appears to be gathering momentum. [REDACTED]

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[REDACTED]

[REDACTED] Import volume, flat for much of 1974, turned down in most countries late last year.

Import prices in national currency units peaked last fall and have since edged downward. The rise in export prices has tapered off; most countries continue to post small month-to-month price increases. [REDACTED]

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[REDACTED] The improved trade balances recently reported by [REDACTED] France stem from better terms of trade.

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In some countries, declining export volume was a major factor in the continued fall of GNP in the fourth quarter. [REDACTED]

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[REDACTED] In other countries, the foreign sector was somewhat stronger in the fourth quarter; [REDACTED]

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[REDACTED]

Note: Comments and queries regarding the *Economic Intelligence Weekly* are welcomed. They may be directed to [REDACTED] the Office of Economic Research, Code 143, Extension 7892.

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**Soviet GNP Growth** of 3.2% in 1974, although below its average rate, compares favorably with growth in the recession-hit West. Increases in the world prices of oil and other Soviet raw materials resulted in a record hard currency surplus in 1974 of about \$1 billion, strengthening Moscow's ability to import Western technology and equipment.

**At the Multilateral Trade Negotiations**, four nontariff barriers (NTBs) have been chosen for initial discussion -- export subsidies and countervailing duties, quantitative restrictions, standards and markings, and customs procedures. Early agreement on these issues, which offer benefits to each of the participants, may provide impetus to further negotiations. The problem of the appropriate forum for the agricultural NTBs has not yet been resolved.

**The OPEC Current Account Surplus** will accumulate to more than \$260 billion by 1977. Only Algeria, Libya, Indonesia, Venezuela, and Ecuador will face balance-of-payments deficits within the next three years; these can be easily financed and will pose no serious internal difficulties. Saudi Arabia will own nearly one-half of the surplus. Saudi funds will be increasingly channeled to foreign government securities, direct loans, equities, and real estate. (Confidential No Foreign Dissem)

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## Articles

## SAUDI ARABIA: NEW DIRECTIONS IN FOREIGN INVESTMENT

Saudi Arabia appears ready to pursue a more aggressive investment policy. While the bulk of foreign assets remain in highly liquid Eurodollar bank deposits, the new Saudi financial leadership is planning to increase the share of investment in government securities, direct loans, equities, and real estate.

## Saudi Arabia: Distribution of Foreign Official Assets

	31 Dec 1973	30 Sep 1974	31 Jan <sup>1</sup> 1975
	Percent		
By type of asset			
Gold and reserve position in the IMF	5	Negl.	Negl.
Bank deposits	65	65	55
Government securities	10	15	25
Nonreserve assets <sup>2</sup>	20	20	20
By location			
United States	15	15	20
United Kingdom	55	55	45
Continental Europe and Japan	25	25	25
IMF and World Bank	5	5	5
Other	Negl.	Negl.	5
By currency			
Gold and reserve position in the IMF	5	Negl.	Negl.
US dollars	70	80	80
British sterling	10	10	10
Other	15	10	10
	Million US \$		
Total foreign assets	4,675	15,044	20,600

1. Preliminary.

2. Primarily government-guaranteed [redacted] and French public utility bonds. Also includes equities and real estate.

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### Traditionally Conservative

Saudi investment practices have traditionally been the most conservative in the Middle East. For 15 years, the cautious Anwar 'Ali headed the Saudi Arabian Monetary Agency (SAMA), which has operational control over essentially all of the kingdom's foreign assets. Despite the massive growth in Saudi official holdings between December 1973 and September 1974, the type, location, and currency denomination of SAMA investments remained largely unchanged. About 65% was held in bank deposits, primarily dollar denominated, largely located in the United Kingdom and the United States.

### Young Technocrats

With Ali's death in November 1974, Saudi financial leadership passed to a group of young technocrats centered around Prince Fahd. King Faysal's appointment of 'Abd al-'Aziz al-Qurayshi as governor of SAMA was a blow to traditionalists such as Finance Minister Musa'id, who had been content to allow Saudi foreign assets to build up in Eurodollar bank deposits. Qurayshi, backed by Aba al-Khayl, Minister of Financial Affairs and National Economy, and Hisham Nazir, head of the Central Planning Organization, wants the Saudis to play a more active role in investment decisionmaking. In any case, the mounting Saudi surplus and the reluctance of international banks to accommodate further short-term funds will compel movement in this direction.

Qurayshi has begun to modify SAMA's internal structure to facilitate this more active investment program. Two new advisory boards will probably be established:

- an investment advisory group, composed of financial experts drawn from Baring Brothers of London and White, Weld and Company of New York, to help SAMA evaluate potential equity and government security purchases, and
- a real estate advisory group, drawn primarily from Morgan Guaranty Trust, to help assess potential real estate investments.

Many transactions will be handled directly by SAMA rather than through major Western banks, as has been the practice until now.

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Qurayshi, who is expected to visit the United States this month, also hopes to begin overseas banking operations. Plans call for SAMA and Morgan Guaranty Trust to open a bank in London this year, with the Saudis having a controlling interest. A SAMA investment office in New York is also being considered.

### Major Decisions

A number of major decisions affecting the distribution of future Saudi investments have apparently been reached, although not yet fully implemented.

- Government securities – SAMA plans to purchase a substantial amount of US Treasury securities -- probably in excess of \$2.5 billion -- through the Federal Reserve Bank of New York during the first half of the year. Additional purchases of US Government and agency securities through commercial banks are expected.
- Equities – SAMA, barring adverse US Government reaction, plans to invest between \$500 million and \$1 billion in US equities this year. Purchases will probably be limited to less than 5% of the shares of any company. (Secret No Foreign Dissem) ■

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### WORLD GRAIN: SITUATION EASES A LITTLE

The world grain situation has eased slightly in the last three months, more so for wheat than for corn.

Although we still forecast 1974/75 grain production (excluding rice) at 6% below 1973/74, prices have fallen because of a sharp decline in grain fed to livestock in the United States. Grain thus has been released to meet foreign demand. Total worldwide grain consumption, however, will not decline as much as production, so that stocks of major producers are expected to fall by more than 20 million tons, to a new low by mid-1975.

### Wheat

We estimate that world wheat production in 1974/75 will be down by more than 20 million tons, or 5.6%. Production declines in Argentina, Australia, Canada,

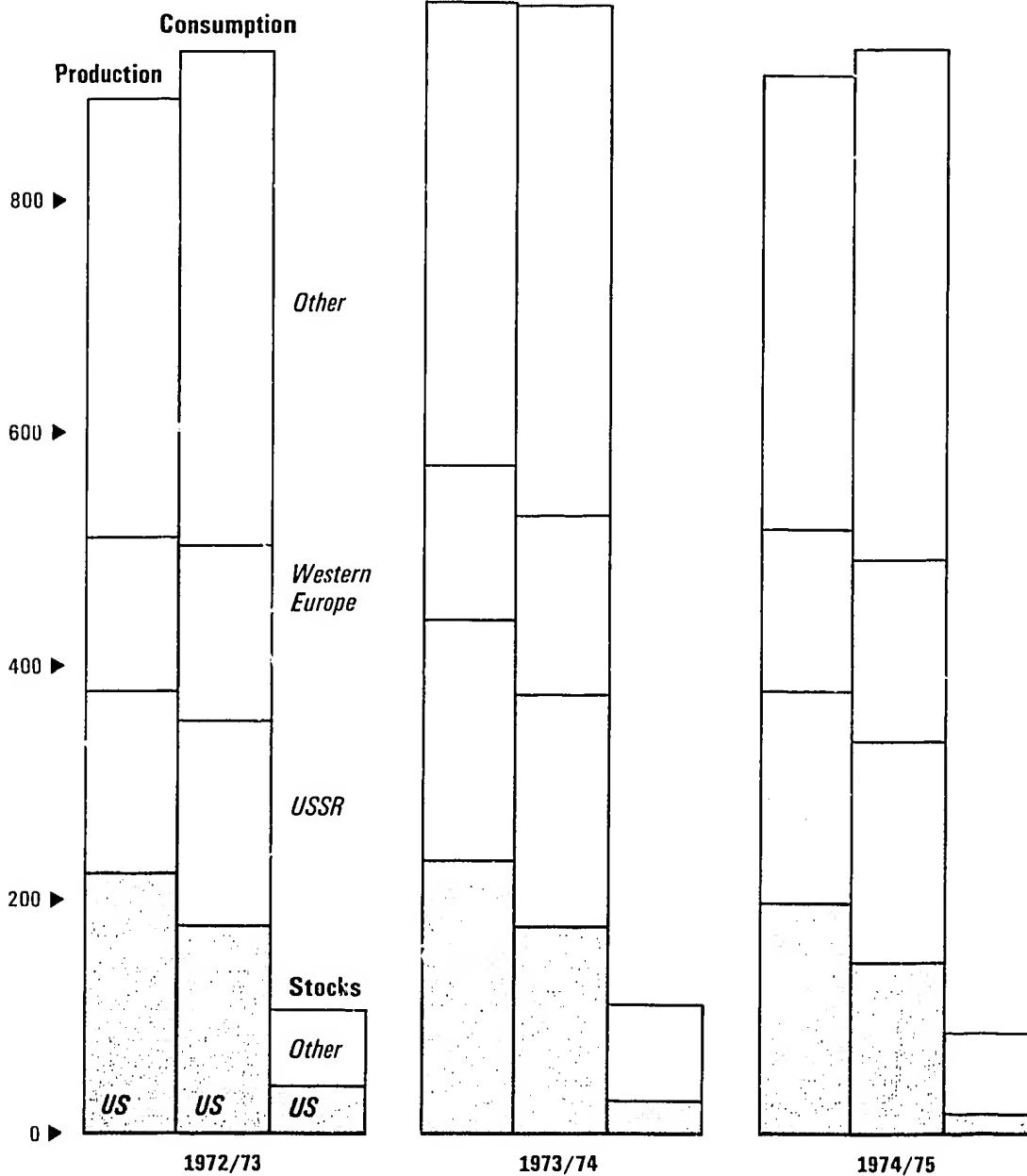


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# **WORLD GRAIN<sup>1</sup>** **Production, Consumption, and Yearend Stocks**

Million Tons

1,000 ►

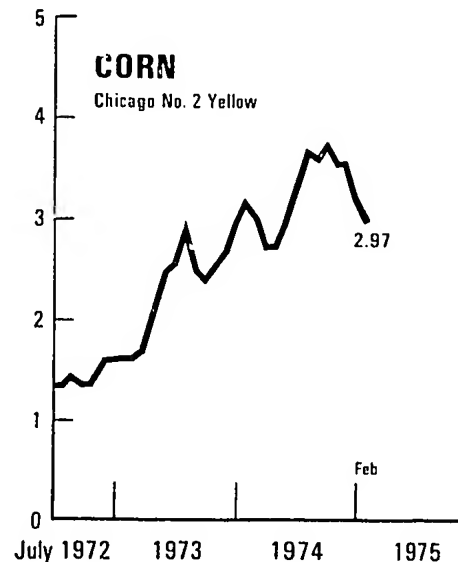
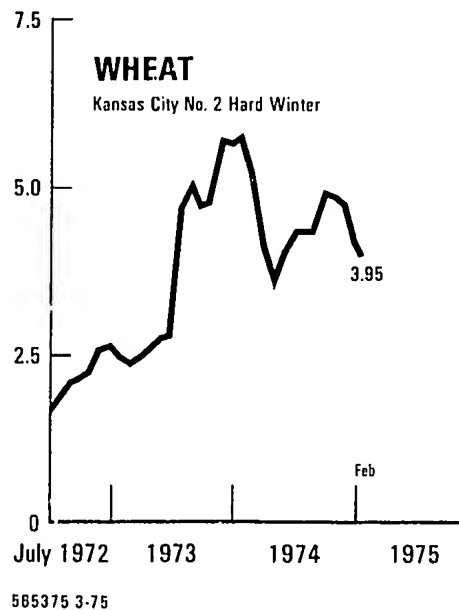


<sup>1</sup>Excluding rice

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## WHEAT AND CORN PRICES \$ Per Bushel (monthly average)



India, and the USSR will not be offset by the bumper harvests in Europe and the United States.

World import demand for wheat is estimated at 65.3 million tons for 1974/75, up 1.3 million tons from our December estimate and 3.4 million tons above exports in 1973/74. Increases in purchases by Brazil, South Asia, Mexico, and northern Africa have more than offset the highly publicized cancellations in recent weeks by the USSR and China.

Wheat available for export could reach 67.6 million tons, or 2.3 million tons above import demand, if the United States and Canada draw down stocks to minimum acceptable levels. This estimate — 3.6 million tons higher than our December estimate — is the result of feeding smaller quantities of wheat to livestock in the EC and of an increase in the US crop. Australia will also have larger quantities available for export than a year ago.

Foreign demand for US wheat and flour is forecast at 31.2 million tons — 200,000 tons above our December estimate and 100,000 tons above 1973/74 exports. This quantity can be exported, assuming that stocks will be drawn down to a record low of less than 5.6 million tons.

### Corn

We estimate world import demand for corn in 1974/75 at 41.8 million tons — 14% more than forecast in December and about the same as in 1973/74. The

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increase in the estimate is due primarily to (a) the replacement of wheat by corn in feeding livestock in the EC, as the result of lower prices for US corn, and (b) crop shortfalls in various East European countries and Mexico. The higher level of demand can be met only if US stocks are drawn down to minimum pipeline requirements and US domestic use continues to decline.

We estimate export demand for US corn at 28.2 million tons, up 4.7 million tons from three months ago. This level of exports is contingent upon a 10% drop in US consumption. The increase is due to foreign buyers taking advantage of falling US corn prices, down 25% since mid-December.

#### Continuing Uncertainties

Current demand for US grain exports could change as a result of the following:

- transport or port problems that periodically interfere with grain shipments from Canada, Argentina, and South Africa;
- the North African drought, which could raise wheat import requirements above current projections;
- the amount of corn substituted for wheat in livestock feeding in the EC;
- the extent of the decrease in US grain feeding; and
- the likely resumption of Soviet corn purchases to take advantage of lower prices. (Confidential No Foreign Dissem)■

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#### SOVIET ECONOMY IN GOOD SHAPE\*

Moscow has good reason to feel more secure about its position in the international economy than ever before.

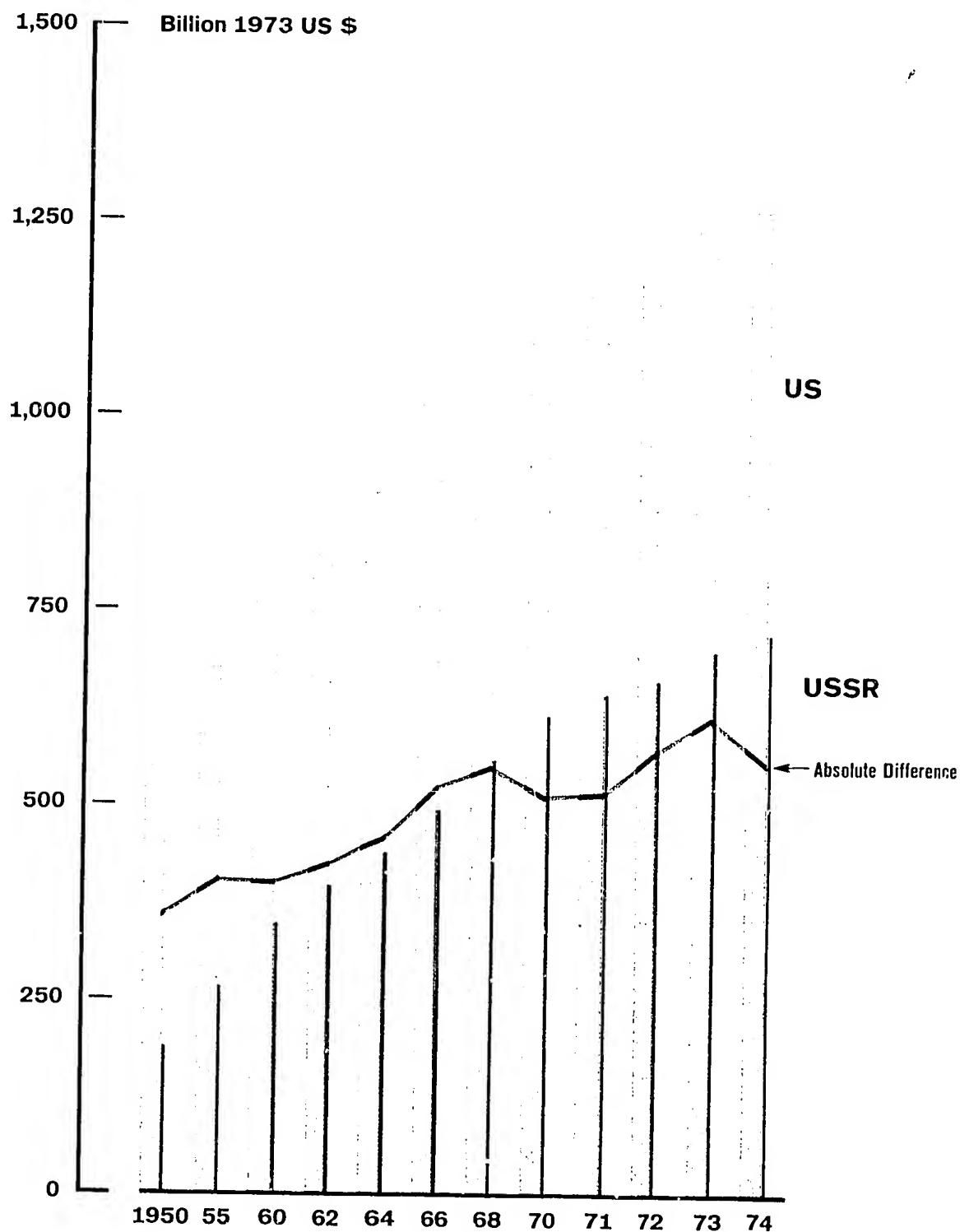
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\* This article presents, in modified form, the conclusions of a forthcoming memorandum, *The Soviet Economy: 1974 Results and 1975 Prospects*.

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# US-USSR: GNP



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Internally, the economy has been growing at a moderate rate, while output is declining in many Western countries. Because of its centrally controlled economy and its economic self-sufficiency, the USSR has been shielded from the recession and double-digit inflation plaguing the West. Thanks to an export surplus in oil and raw materials, the Soviet balance of payments has benefited from high world market prices. But basic problems of low efficiency and an inability to quickly apply new technology remain, and Moscow cannot readily translate its temporary advantages in dealing with the West into remedies for its long-term economic ills.

#### Developments, by Sector

Soviet GNP grew by 3.2% in 1974, less than half the pace of the previous year, but far ahead of most other industrialized countries. The gap between the GNP of the United States and the USSR declined by a record \$50 billion.

- A slump in farm output caused by poor weather was the major cause of last year's slowdown. Still, agriculture enjoyed its second best year; grain output at 195.6 million tons was the second highest in Soviet history, and cotton production reached a new peak. Moscow bought only 6-1/2 million tons of Western grain for delivery in fiscal year 1975 and carried over large grain stocks from the 1973 record harvest.
- Industrial output -- the economic bellwether of the leadership -- grew at its highest rate since 1970. Adequate supplies of raw materials and energy were major factors in this growth as well as larger than planned additions of new workers and the highest rise in labor productivity in the current five-year plan period. The leading growth sectors -- energy, producer durables, chemicals, and processed foods -- reflect the leadership's priority for technological advance and for expansion of farm output.
- Consumer welfare continued its steady rise, featured by increased availability of meat and dairy products, soft goods, and automobiles. Full employment continued, and prices were stable, although, as usual, not all goods and services were available at official prices. Housing continues to be the area of greatest consumer dissatisfaction.
- The hard currency surplus reached \$1 billion last year, compared with the nearly \$1 billion average *deficit* in 1970-73; price increases for Soviet oil and other raw materials far outweighed price increases for imports.

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Trade with the West boomed, growing by almost 48% and accounting for 31% of total Soviet foreign trade. Soviet machinery orders from the West reached a record \$4.1 billion -- a 78% rise over 1973.

USSR: Growth of GNP, by Sector of Origin<sup>1</sup>

	Percent					
	Average Annual 1966-70	1971	1972	1973	Prelim- inary 1974	Plan 1975
Gross national product, by producing sector	5.5	4.2	1.8	7.5	3.2	7.0
Agriculture <sup>2</sup>	4.6	0.1	-7.0	16.4	-3.3	10.8
Industry	6.8	6.5	5.6	6.2	6.8	6.7
Construction	7.0	8.7	6.4	2.2	5.0	6.5
Transportation and communications	6.2	6.6	4.9	7.3	6.6	7.0
Domestic trade	8.2	6.8	6.9	5.4	5.9	7.2
Services	4.4	4.0	4.2	3.7	3.7	4.4

1. Calculated at factor cost.

2. This measure of agricultural output excludes intra-agricultural use of farm products but does not make an adjustment for purchases by agriculture from other sectors. Value added in agriculture grew by an average of 4.1% in 1966-70, 0.6% in 1971, -9.1% in 1972, 16.5% in 1973, and -5.2% in 1974.

## Plan for 1975

The Soviet plan for 1975 optimistically anticipates that GNP will grow at more than double the 1974 rate. This high rate depends on a large boost in farm output and a matching of last year's industrial growth. So far this year the weather has been favorable for winter grains, making a record crop possible. Moreover, history shows that good winter crops are usually followed by bumper spring crops. The industrial plan may be more difficult to fulfill. According to Soviet statistics, industrial output in January grew only 6.7% (compared with January 1974), whereas output in January 1974 grew 9.6% (compared with January 1973).

The Soviet hard currency surplus in 1975 probably will match the \$1 billion earned in 1974 as the Soviets continue to benefit from raw materials exports. This financial cushion will allow them to pay cash for some purchases, resist high interest rates, and postpone exports of some commodities that will bring higher prices in the future. Soviet renunciation of the US-Soviet trade agreement will have little impact on trade in 1975.

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### Commitment to Consumer

Although many original consumer targets for 1975 will not be met, because of disappointing harvests and lagging construction, Moscow remains firm in its commitment to raise living standards. Support for the agricultural sector, an important prerequisite for satisfying consumer demands, continues high this year; agricultural investment will be a record percentage of total investment, and industrial deliveries to the farms are scheduled to increase at a fast pace. Also, machinery branches that supply equipment to the agricultural sector and to the light and food industries will continue to expand briskly. (Unclassified) ■

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### FRANCE: RECESSION HELPS CUT PAYMENTS DEFICIT

The French balance of payments will improve sharply in 1975, the result largely of the stagnation of imports and massive OPEC orders for machinery. The current account deficit will shrink to a level that can be financed from normal capital inflows without drawing down reserves or borrowing from the new special recycling funds.

#### Outlook for the Current Account

We estimate the 1975 current account deficit at \$4.1 billion, down from the \$5.8 billion of 1974. The trade deficit should drop by \$2.0 billion – to \$1.5 billion. Net invisibles outflows will edge up slightly to about \$2.6 billion. Rising interest payments will more than offset a decline in worker remittances as unemployed foreign laborers return to their homelands.

The oil deficit will probably rise slightly, to about \$9.3 billion. Domestic oil consumption should be stable at the 1974 level. Because imports exceeded consumption last year, a cut in import volume of 3% seems likely. This cut will be more than offset by a higher average price for oil.

We expect the non-oil trade surplus to increase by two-fifths, to an estimated \$7.8 billion. Slow growth in economic activity among France's trading partners -- less than 1% on a trade-weighted average -- will hold the expansion of export volume to only 2%. This effect will be more than offset by the sharp French recession. Industrial production has plummeted 11% since August and for 1975

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## France: Current Account Balance

Billion US \$

### Oil Trade f.o.b.

1973	1974	1975
-2.3		
	-9.0	-9.3

### Non-Oil Trade f.o.b.

1973	1974	1975
3.7	5.5	7.8

### Net Services and Transfers

1973	1974	1975
-2.1	-2.3	-2.6

### Total Current Account

1973	1974	1975
-0.7		
	-5.8	-4.1

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as a whole should be slightly below the 1974 average. This slowdown has been reducing import demand while freeing capacity to serve export markets.

The gain in the non-oil surplus will be held down by the somewhat reduced price-competitiveness of French goods. We expect the franc to appreciate in 1975 in relation to the currencies of France's trading partners. Partly offsetting this will be a French inflation rate probably somewhat below the weighted average of its trading partners. Overall, terms of trade should improve by 3%-4% in 1975.

The trade balance in capital goods should conspicuously improve. Traditionally in deficit, this sector recorded a small surplus in 1974 and - boosted by huge OPEC orders for a wide variety of industrial projects - should do much better this year. The favorable trade balance in agricultural products should continue to mount. The deficit on nonenergy raw materials probably will fall slightly because



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of (a) the domestic industrial slowdown and (b) a 24% drop to date in the prices of imported raw materials, compared with January 1974.

#### Financing the Deficit

France should have no problems financing its current account deficit in 1975. A larger deficit was covered last year without difficulty; in fact, Paris managed to increase its exchange reserves by \$0.3 billion during the year without resort to official borrowing. Long-term borrowing by French firms – particularly state-owned ones – brought in perhaps \$2.5 billion, after Paris reversed its earlier policy of discouraging such loans. A Treasury loan attracted another \$0.8 billion from abroad, and the remainder of the inflow was largely short-term capital. The capital flow from OPEC countries is estimated at more than \$3 billion, including \$0.3 billion in advance payments from Iran.

Most of the 1975 deficit will again be covered by long-term borrowing by French firms. In contrast with Britain and Italy, France has a sound international credit rating because of confidence in its economy and currency. Direct investment and portfolio investment will make only a small contribution, as most of this inflow will be offset by French investment abroad. The remainder of the current account deficit will probably be financed by short-term private capital inflows.

Further large capital flows from OPEC are certain. Good relations with the oil producers, coupled with the strength of the franc, make France an attractive repository for OPEC funds. The money will again consist largely of advance payment for equipment and loans to the French government and nationalized industries. Little direct OPEC investment is in prospect for 1975. (Confidential)

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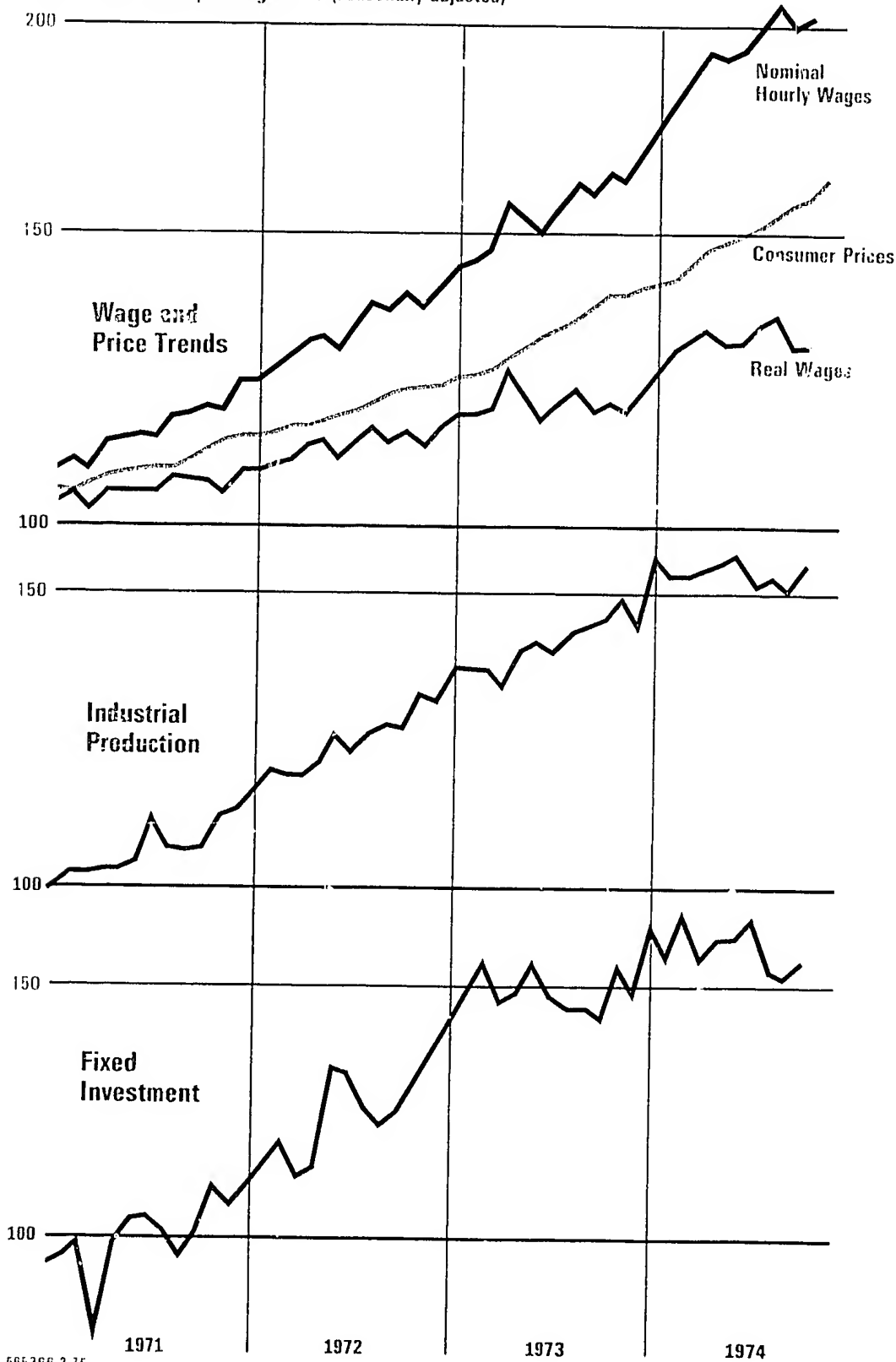
#### SPAIN: STRESSING GROWTH, ACCEPTING INFLATION

Prime Minister Arias is trying to maintain economic expansion in the face of international recession. He is in trouble: output has risen at a slower pace since last summer, inflation has approached a 20% annual rate, a drop in real wages has spawned strikes and demonstrations, and a big current account deficit has opened up. We expect Arias to continue to stress growth while accepting inflation and a sizable current account deficit.

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# SPAIN

Index: 1970 monthly average = 100 (seasonally adjusted)



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Spain: Balance of Payments

	Million US \$			
	1971	1972	1973	1974 <sup>1</sup>
Exports	2,980	3,920	5,340	7,100
Imports	4,580	6,240	8,840	14,400
Trade balance	-1,600	-2,320	-3,500	-7,300
Services, net	1,690	2,020	2,650	3,000
Of which:				
Tourism	1,880	2,230	2,840	2,800
Transfers, net	770	870	1,400	1,100
Current account balance	860	570	550	-3,200
Long-term capital, net	500	930	760	1,500
Basic balance	1,360	1,500	1,310	-1,700
Errors and omissions	-100	40	30	-100
Short-term capital	0	-50	200	800
Other	180	10	-320	200
Change in reserves	1,440	1,500	1,220	-800

1. Estimated.

### Recent Developments

The Spanish economy lost momentum in the second half of 1974. The higher cost of oil and other imports drained away huge sums at the very time that tourism was faltering and worker remittances were falling off. A moderately expansionary fiscal package enacted last March was insufficient to offset the impact of these external forces. Furthermore, consumer demand was eroded by accelerating inflation, and business confidence was undermined by General Franco's illness and uncertainties surrounding the succession.

Rapid expansion of investment early in 1974 helped keep GNP growth to 5% for the year as a whole. Although this was not too far below the 7% annual average of the preceding decade, by yearend the economy was expanding at an annual rate of only 2%-3%.

As economic growth slowed, unemployment rose -- officially to 1.8% of the labor force in December -- up from 1.2% a year earlier. In reality, unemployment probably was double the admitted rate. Worker unrest, heightened by inflation, increasing job insecurity, and return of workers from abroad has brought a wave of strikes and demonstrations. Although strikes still are illegal, Madrid initially reacted with moderation, reportedly advising employers it would tolerate wage

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increases as high as 30%. As disorders intensified in January and February, the authorities cracked down.

Consumer prices rose 18% in 1974 – about 4 percentage points more than in the OECD countries as a whole. Prices had begun to soar in the second quarter of 1973. As elsewhere, higher prices on imported oil, foodstuffs, and raw materials were a major influence. Madrid's reluctance to dampen economic activity allowed inflation to go unfettered.

The balance of payments deteriorated throughout 1974. The higher prices paid for oil and other imports were a major factor. Outlays for crude oil jumped \$2.3 billion. Drought hurt trade in agricultural products on both the import and export sides. Continuation of rapid industrial growth into the first half of 1974, combined with domestic inflation, brought a substantial increase in import volume. Declines in tourist receipts and worker remittances contributed to the \$3.2 billion current account deficit. Government-controlled corporations helped protect the country's reserves by borrowing \$900 million on the Eurocurrency market instead of obtaining funds from the usual domestic sources. Private short-term borrowing abroad drew in additional money. Foreign reserves nevertheless fell by \$800 million to about \$6 billion.

#### Outlook

The Arias government will continue to tolerate a big current account deficit and rapid inflation rather than impose austerity measures. We expect real GNP to grow by 2%-3% in 1975, not enough to absorb the natural increase in the labor force, the drying up of foreign jobs, and the continuing improvement in labor productivity. Inflation will ebb only slightly and will continue to erode recent wage gains. Further labor unrest seems guaranteed. (Confidential) ■

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#### YUGOSLAVIA: BALANCE-OF-PAYMENTS DIFFICULTIES

Prime Minister Dzemal Bijedic will arrive in Washington on 19 March to meet with the President and Cabinet officials on trade and financial matters. Yugoslavia can expect more acute balance-of-payments difficulties in 1975 as hard currency earnings shrink because of the Western recession.

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### Payments Deficit

Trade was hit hard in 1974 by the economic slump in the West, the EC ban on meat imports, and higher import prices. Terms of trade deteriorated as import prices climbed 46% while export prices rose only 32%. Oil imports alone cost \$600 million more because of higher prices. The hard currency trade deficit was a record \$2.7 billion, compared with \$1.2 billion in 1973.

Worker remittances and tourist earnings, which had offset the trade deficit in 1972 and 1973, fell short in 1974. The resulting \$1 billion current account deficit was financed by supplier credits, bank loans, and a \$200 million drawdown of foreign exchange reserves. With reserves at only \$1.3 billion – the equivalent of two months' imports – Bijedic announced in December that the 1975 deficit would have to be covered by borrowing abroad.

### Rise in Debt Payments

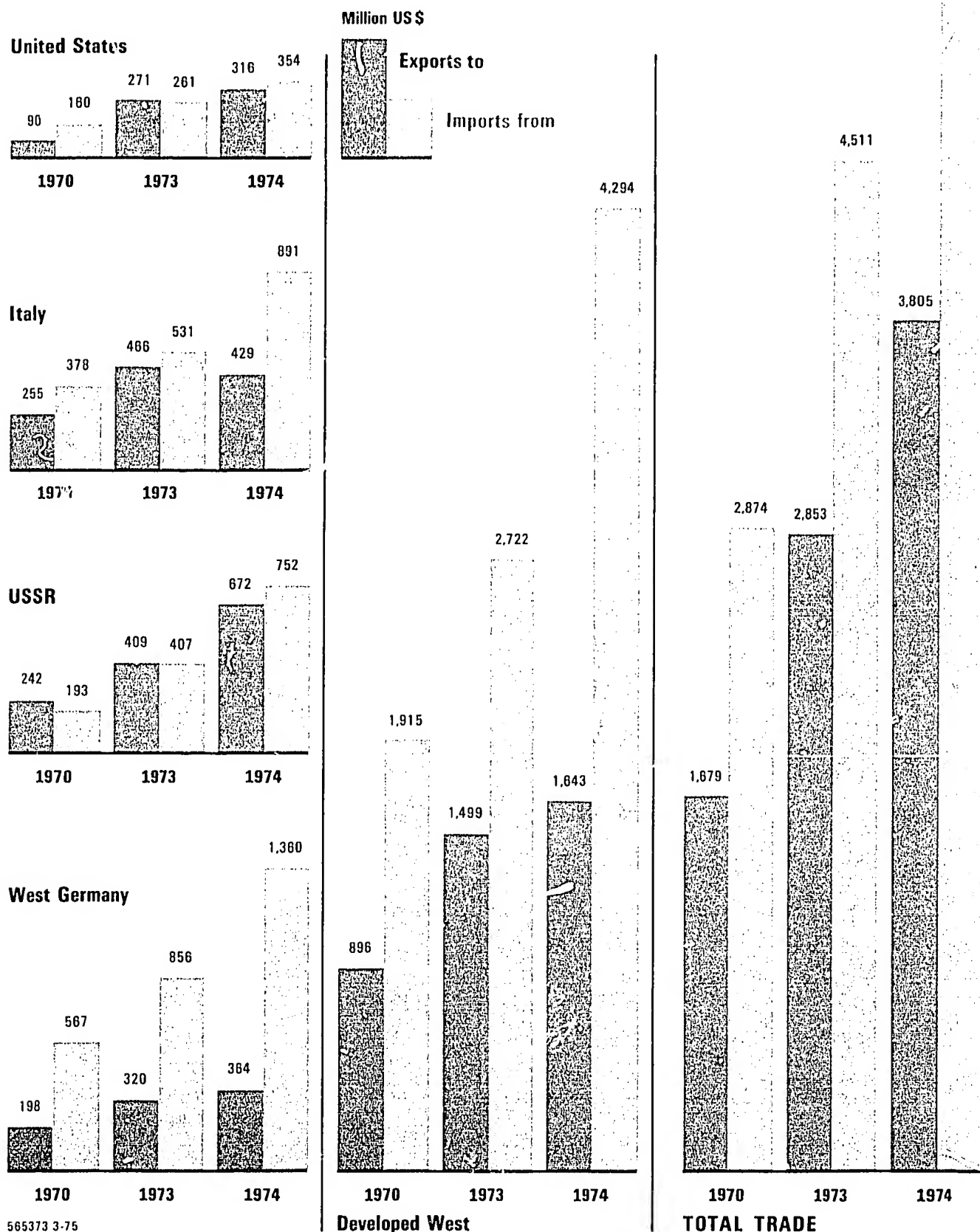
Annual debt service payments have been manageable since Belgrade arranged debt rescheduling with important Western creditors in 1971. The borrowing required to finance last year's deficit, however, sharply increased the schedule of debt payments for the next several years. The hard currency debt is now about \$4-1/2 billion, with known debt to the United States accounting for one-tenth. Belgrade is the US Eximbank's largest customer in Europe; a loan in August 1974 involved \$176 million for the Krsko nuclear powerplant, to be built by Westinghouse.

### The United States as Fourth Largest Trading Partner

West Germany is still the leading trading partner, with the USSR, Italy, and the United States following in that order. Traditionally, Yugoslavia has purchased more from the United States than it has sold. It buys mainly agricultural products (wheat and feed) and transportation equipment (mostly aircraft). Sales to the United States include processed foods, nonferrous metals, furniture, and wine. To reduce its hard currency expenditures, Belgrade has promoted joint equity ventures with US firms. Apparently because of Yugoslav restriction on profit repatriation, probably less than \$50 million had been invested in such ventures by yearend 1974. In a major new development, Dow Chemical Company signed a preliminary agreement in January 1975 for a \$500 million joint equity petrochemical project.

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# YUGOSLAVIA: Foreign Trade



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### Rapid Growth in 1974

The rapid growth in import volume in 1974 helped sustain domestic economic momentum. GNP increased by an estimated 6%; industrial production 10%; and agricultural production 3%, aided by a record wheat harvest. At the same time, inflation rose to 25% – compared with 19% in 1973 – a reflection of large wage increases, duplicative investment, delays in the commissioning of new industrial capacity, and rises in import prices.

### Developments in 1975

The rapid economic expansion is tapering off. Growth in industrial production is targeted at only 7% in 1975. The government has introduced austerity measures, including restriction on imports, to cope with inflation and the payments deficit. Unemployment already is rising, worsened by the return of workers from abroad.

To ease its payments situation, Belgrade plans to issue bonds on the international market with 10- to 20-year redemption periods. Meanwhile, exports to the West in February were below the previous year's level, and return of Yugoslav workers from Western Europe continues with the expiration of work contracts. (Confidential)■

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### Publication of Interest\*

The Economic Situation in South Vietnam, February 1975  
ER IR 75-8, March 1975 (Confidential No Foreign Dissem)

This edition of the monthly economic report discusses (a) seasonal price increases brought about largely by the Tet celebrations, (b) continuing disappointing export receipts, (c) a second promising oil discovery, (d) lack of substantial impact on rice production of Communist military and economic activities, and (e) development of Saigon's Export Processing Zone.

\* Copies of this publication may be ordered by calling [REDACTED] Code 143, Extension 7234.

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